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C O N F I D E N T I A L SECTION 01 OF 03 HONG KONG 000930

SIPDIS

STATE FOR EAP/CM AND EEB/TPP
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SUBJECT: U.S. CONSUMER PRODUCT SAFETY LAW RESHAPING TEST
LABS' BUSINESS MODELS

REF: A. HONG KONG 649

[1](#)B. 2008 GUANGZHOU 146

Classified By: Consul General Joe Donovan for reasons 1.4 (b) and (d)

[1](#)1. (C) Summary: During May 13-14 tours of three consumer product testing labs in Hong Kong and Dongguan that examine children's products bound for the United States, lab company managers said enactment of the U.S. Consumer Product Safety Improvement Act of 2008 (CPSIA) had boosted their testing revenues by "double digits." They described challenges posed by CPSIA-related regulations including: "inexact" definitions regarding what constitutes a children's product or toy; lead content testing guidelines from the U.S. Consumer Product Safety Commission (CPSC) that result in "over testing" of the colored coatings and printing materials used in children's products; and insufficient coordination and synchronization of product safety standards among U.S. states, the USG and other major international consumers such as the European Union. They described an ongoing shift of testing resources from Hong Kong to the Mainland, as they and other testing companies build a base of qualified Mainland technicians and field staff capable of maintaining testing standards. One of the companies described its internal audit processes, saying it fires "single digits" of its Mainland field staff each calendar quarter on suspicion of accepting bribes from manufacturers. End summary.

[1](#)2. (C) Comment: Consumer product testing firms deal extensively with both local manufacturers and the companies importing consumer goods (especially children's products) into the United States. They therefore provide unique, market-encompassing insights into the CPSIA's impact in Guangdong and Hong Kong. The testing companies confirmed our sense that local criticism of the CPSIA has declined in recent months, as regulations and implementation timelines have become more detailed and widely disseminated. Testing firms also said compliance uncertainties surrounding CPSC regulations are increasingly viewed as manageable by medium and larger-sized manufacturers in Guangdong. Given the additional regulatory complexities associated with product safety regulations in various jurisdictions, manufacturers and importers are beginning to rely on product testing companies for advice, not just related to final product testing requirements, but also with regard to product design, manufacturing processes and supply chain management.

Background

13. (U) EconOffs from Consulates General Guangzhou and Hong Kong jointly met on May 13 and 14 with two major consumer product testing companies in Hong Kong and Dongguan (Guangdong Province's third-largest city), including tours of three test labs. Each company and its labs have been certified by the CPSC as suitable for examining the safety of consumer products to be exported to the United States.

Product Testing Labs Benefit From CPSIA

14. (SBU) Executives from Bureau Veritas (BV) and Modern Testing Services (MTS) said the CPSIA compelled manufacturers, retailers and importers of consumer products to increase the frequency and scope of testing of products destined for the U.S. market. BV and MTS managers said all the major product testing companies (including other major players such as Intertek and SGS) have benefited from the CPSIA's new safety standards and certification requirements. BV Director of Technical and Engineering Services Travis Norton (an American citizen working over nine years for BV in Hong Kong) said the CPSIA continues to drive BV's "double-digit" revenue growth from testing toys and juvenile products. The global economic downturn had thus far not materially impacted product testing revenues in Southeast China. "The volume of exports to the United States has declined, but product diversity has not," Norton said. To

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further boost revenues, both BV and MTS increasingly serve as CPSIA compliance advisors to manufacturers who request examinations of product designs, supply chain integrity and production processes. Both companies said they have sufficient testing capacity to handle Christmas-related export surges.

Triple-Layered Toy Testing

15. (SBU) BV is a publicly-traded testing company headquartered in Paris. BV's China operations are headquartered in Hong Kong, with two labs in Hong Kong, three in Guangdong and one in Shanghai. In describing the effects of the CPSIA on major U.S. toy brands, BV Technical Consultation manager Maggie Wang said toy companies such as Mattel and Hasbro are pre-testing their products, before the products are sent to CPSC-approved third-party labs such as BV. In addition, manufacturers often add a third layer of protection by self-testing their own products, in addition to whatever tests are performed by the importer/retailer and the external labs (septel describes this process). Norton criticized the testing redundancies of this approach. He said, "We're still dealing with the 1980s model (of testing finished products). The U.S. government must encourage product testing programs that focus more on certifying raw materials, product designs and factory production processes." He described this as "a holistic, upstream approach that will result in fewer recalls and safety problems with final products."

16. (SBU) Norton said BV will relocate to Mainland China as much of its Hong Kong-based operations as possible, in order to reduce operating costs. He said this shift would occur only gradually, in line with improvements in the technical expertise of China-based staff. "It's hard to find and keep highly qualified technicians in the Mainland," he said.

CPSIA-Related Testing Challenges

17. (SBU) MTS Managing Director and Co-Founder Byung Won Park started his firm in 2006, following expiration of a 5-year

non-compete agreement with BV. Park sold his previous consumer product testing firm to BV in 2001. Park said his firm's revenues are growing more than 50 percent on an annualized basis, with labs in Hong Kong, Dongguan and Shanghai. Like BV, MTS provides customized interpretations for its customers of the CPSIA and its related CPSC regulations, in addition to his firm's standard safety and performance testing services. According to Park, MTS seeks to differentiate itself through its consultancy services and the company's internationally educated management team.

18. (SBU) Park met EconOffs at MTS' large new lab in Dongguan that is gradually ramping up operations. He described some of his customers' CPSIA-related challenges. He said, "Sometimes the CPSC has not clearly defined what is, and what is not, a children's product or toy that is subject to stricter testing and safety requirements." He said this causes consternation among manufacturers and retailers selling products in the United States. Chinese manufacturers routinely ask MTS for advice and then generally adopt the most conservative interpretation and testing regime for any U.S.-bound product.

19. (SBU) Park also said the CPSC "should provide common sense regulations concerning color testing for lead content." Park cited the example of labs conducting "excessive" testing for lead on the infinite array of colors used in toys and their packaging. Park said the CPSC should issue a regulation designed to ensure the safety of the five primary colors used in any production process, thereby obviating the need to test each color combination derived from use of one or more of the primary colors. He said, "We shouldn't need to test 30 different colors used on a given product." (Note: During visits to three product testing labs - BV and MTS in Hong

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Kong, and MTS in Dongguan - EconOffs noticed a significant proportion of lab staff members engaged in scraping various color samples off children's products and their packaging. End note.)

110. (SBU) Park encouraged the CPSC to boost cooperation with its EU counterparts to synchronize consumer product testing regulations (ref B). He also noted that some U.S. states have adopted stricter children's product safety standards than those contained in the CPSIA. He cited the example of Illinois' new requirement (to take effect in January 2010) for warning labels on children's products coated with paint containing more than 40 parts per million of lead. CPSC's latest CPSIA-related regulations will allow the sale of children's products with paint containing up to 90 parts per million with no warning required. Park described how manufacturers have been forced to adjust their consumer product production processes and labeling to meet the combination of strictest requirements in all jurisdictions where a product is sold. He described this as a necessary but expensive approach to produce to the "highest common safety denominator." Park said increased intra-USA and international standardization of product content and testing regulations would significantly lower testing costs and enable price reductions in U.S. retail stores, without reducing product safety.

Internal Audits Ensure Integrity of Testing Process

111. (C) BV's Norton described his company's efforts to ensure the integrity of product testing results. These include significant expenditures - and management focus - on internal audits focused on BV's Mainland field staff. Norton said BV terminates "single digit" numbers of field staff each quarter for accepting cash or other favors from manufacturers who attempt to manipulate the product testing process. Norton said this is down from "double digit" corruption-related field staff firings only two years ago, due to BV's increased focus on field staff member audits. He described a recent

example of internal corruption, as follows.

¶12. (C) A major U.S. retailer asked BV to randomly select product testing samples from a manufacturer in Guangdong, prior to accepting the manufacturer's goods and importing them into the United States. A BV field staff member was assigned to visit the factory, collect the random samples and deliver them to BV's testing facility. To ensure satisfactory test results, the manufacturer bribed the visiting BV staff member to accept and deliver only manufacturer-selected product samples for the testing lab. Norton said smaller testing firms that use contractors to collect product samples face even greater corruption-related challenges in China. He said, "We have a large bureaucracy in place, and it hurts our margins, but BV's long-term success is based on the accuracy and integrity of our test results."

¶13. (U) This cable was produced cooperatively with, and cleared by, Consulate General Guangzhou.
DONOVAN